

# SPONSOR'S REBUTTAL TO FISCAL NOTE

Bill Number:

SB 260

Date Prepared:

Short Title:

EXHIBIT

2

Sponsor:

Gillan

DATE

4-9-09

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Fiscal Note Version and Date:

**Generally, why do you disagree with the fiscal note?**

The Department makes several assumptions that are flawed in its fiscal note and fails to account for a new tax on partners aimed at recapture of depreciation and depletion that is included in the bill.

Under the proposal, the Department will receive specific information on all partners who have the most income attributable to Montana sources. The information will be provided in the easiest and most efficient way to confirm, compare and audit the hundreds of thousands of limited partners with potential income. Instead of having to sort through hundreds of thousands of limited partners' tax returns, the Department will be able to simply match several hundred tax ID numbers. This will result in a significant savings to the Department from a compliance standpoint.

It should also be noted that the partners owning the largest shares of PTPs, the general partners, are already in compliance, filing returns, paying and remitting tax as required (their returns are subject to audit at any time by the Department). Based on partnership K-1 data provided to us by PricewaterhouseCoopers, the leading tax processor for PTPs, the vast majority of the limited partners (84%) receive net losses each year. Of those partners with income attributable to Montana, only 199 (or .09%) have any significant enough amount of income to result in a tax liability of \$40 or more per partner.

Under the legislative proposal, the Department will receive more information than ever before, customized to the Department's needs, specifically targeting those partners with the most significant income. This should result in additional compliance with the Montana tax law as well as a reduced burden on the Department's administration of the provisions.

The Multistate Tax Commission included an exclusion for PTPs which meet certain conditions in its model legislation relating to withholding for nonresidents. A copy of this model legislation is attached for your review.

It should also be noted that 31 other states have adopted the model statute recommended by the Multistate Tax Commission. This is the first time a negative fiscal impact has ever been attributed to this proposal.

Level of Montana Income	Number of Unitholders	Percentage of Partners	Total Income for Category	Percentage of Total Montana Income	Average Income Per Partner
Less than \$0	172,933	84%	<-11.060.769>	0%	<-\$63.96>
\$0 to \$500	32,548	15.9%	\$418,328	18%	\$12.85
More than \$500	199	.09%	\$1,864,536	82%	\$9,369

The outcome of the survey demonstrates that fewer than one-tenth of one percent of PTP partners are responsible for more than 82 percent of income attributable to Montana.

**Department Position:**

"The PTP tax liability was estimated to be about \$2.0 million for tax year 2006. The estimated revenue loss from the proposed provision allowing exclusion of those with less than \$500 of Montana source income from the information return is \$500,000 per year (25% of \$2 million)."

**Response:**

Using the information provided by PWC to estimate the potential tax liability of the unitholders with income of less than \$500 would result in total Montana income of \$418,328. If this amount was taxed at the maximum Montana income tax rate of 6.9 percent, it would result in a tax liability of approximately \$29,000, not \$500,000.

Additionally, the Department assumes that no partner with less than \$500 of Montana source income will actually file a Montana return and pay their appropriate amount of income tax. The calculation by the Department also does not account for a new tax created under the legislative proposal to recapture depreciation and depletion when partners sell their interest in a PTP.

**Department Position:**

"On page 4 of the amended bill, part (7) states that the PTP who files an annual information return reporting the name, address and taxpayer identification number for each person or entity that has an interest in the partnership will provide it in electronic form capable of being sorted and exported. The potential cost to the state of compliance activities using this proposed information return would be reduced if the information return also provided the income and Montana apportionment information. DOR also recommends that the language be modified to require the filing to be in a format determined by the department in order to minimize additional compliance costs."

**Response:**

The PTP will provide the name of each partner, known address, taxpayer identification number, and the amount of Montana source income of those partners with Montana source income of more than \$500, or those who sell their units, in the annual report filed with the Department.

**Department Position:**

"The alternative informational filing proposed in this bill may increase the costs of compliance due to the need to research the possible Montana tax liability and, if necessary, contact individual taxpayers. Conversely, the alternative informational filing and revision of Montana source income

proposed in this bill may increase collections.”

**Response:**

The Department will receive all information necessary to identify those partners with the most significant income, and essentially anyone that would have a potential tax liability of more than \$40. This will ensure the ability of the Department to collect the appropriate tax.

As stated above, this proposal also creates a new tax on partners when they sell their units of a PTP, which will also generate tax revenue to the State.

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**What is your estimate of the fiscal impact (approximately)?**

While it is difficult to determine the fiscal note attributable to this bill, we are confident that it will result in a positive fiscal impact to the state because of:

- More accurate, specific and detailed information being provided to the State on any unitholder that receives more than \$500 worth of income or who sells their shares in the PTP during the year
- The proposal creates a new tax on those partners who sell their interest in a PTP during the tax year. The tax will be on the recapture of depreciation and depletion under IRC Section 751 apportioned to Montana. That amount of recapture of depreciation and depletion will be taxed according to Montana income tax rates.

Both of these provisions will ensure that Montana is receiving more information about those who owe income tax while also relieving the Department of potentially significant compliance burdens.

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**Specifically, what in the fiscal note do you feel is flawed?** *[Describe specific assumptions, calculations, technical issues, etc.]*

**Department Position:**

“Owners of the publicly traded shares of publicly traded partnerships may not be aware of the source of the income they receive from their partnership interest, and therefore may be incorrectly paying tax on this income to their home state rather than to the income source state.”

**Response:**

Partners receive an annual K-1 that clearly outlines income attributable to each state. However, very few partners are credited with net income. The income generated by the partnership is apportioned among all of the states where the partnership conducts business and then among tens, if not hundreds, of thousands of unitholders. The amount of allocated income is also dependant on what the cost of the unit was when each individual partner purchased their units as well as the length of time the partner has owned their units. (Please see the example below for more specific information.)

**Department Position:**

“The bill allows PTPs who provides records of ownership for those owners who have more than \$500 in Montana source income to be exempt from filing a composite return.”

**Response:**

While the bill provides an exemption for PTPs from filing a composite return and withholding, it does not provide an exemption from any person or entity paying their appropriate amount of Montana income tax. As noted above, PTPs provide partners with information on the states to which their income is allocated and encourage them to comply with state tax laws. Providing the State with a comprehensive list of partners who are allocated \$500 or more in Montana source income during the year will account for the vast majority of income attributable to Montana, and thus the State will be able to easily determine whether a partner has remitted the appropriate return and any necessary tax payment.

**Department Position:**

“Discussion with industry representatives and review of K-1 tax reporting records indicates that owners with less than \$500 in Montana source income are allocated between 10% to 40% of the PTP’s Montana source income. This fiscal note estimates that owners with less than \$500 in Montana source income represent 25%  $((10\%+40\%) / 2)$  of Montana source income and subsequent state income tax liability.”

**Response:**

Very few unitholders (partners) of PTPs are allocated net income during the year. PricewaterhouseCoopers (PWC) conducted a survey on behalf of the PTPs for the Multistate Tax Commission in 2003. The survey showed that those partners with Montana source income broke down in the following manner: